



## Sunac (1918 HK)

### A new adage: high gearing for high growth

- Sunac's 10M17 presales surged 142% YoY to RMB 249bn, higher than the average peer growth of 45% YoY
- 71% of Sunac's landbank was acquired via M&A. Average land cost of RMB 5,130/sqm represents 30% of Sunac's 10M17 presales ASP
- Average daily turnover of Sunac's shares was ranked no.2 among the HK-listed PRC property stocks
- Upgrade to **BUY** from Sell with revised TP of HK\$ 42.20 (from HK\$ 9.70) based on a 30% discount to NAV

## Company Report

Nov 14, 2017

Rating: **BUY**

TP: HK\$ 42.20

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Share price (HK\$)	36.45
Est. share price return	15.7%
Est. dividend yield	1.3%
Est. total return	17.0%
Previous Rating & TP	SELL, HK\$9.70

Previous Report Date May 17, 2017

Source(s): Bloomberg, ABCI Securities

#### Key Data

52Wk H/L(HK\$)	43.55/5.31
Issued shares (mn)	3,857
Market cap (HK\$ mn)	146,472
3-mth avg daily turnover(HK\$ mn)	962.88
Major shareholder(s) (%)	
SUN Hongbin	50.89%

Source(s): Bloomberg, ABCI Securities

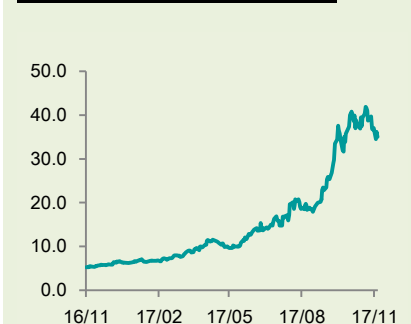
#### Share Performance

	Absolute	Relative*
1-mth	(11.3)	(13.2)
3-mth	92.8	78.0
6-mth	254.6	206.0

\*Relative to HSI

Source(s): Bloomberg, ABCI Securities

#### 1-Year share performance(HK\$)



Source(s): Bloomberg, ABCI Securities

**Quantum leap in presales since 2H17.** Sunac's presales growth exceeded 100% YoY for five consecutive months since June 2017. In particular, the monthly figure hit RMB43.0bn (+218%YoY) in Sep 2017 and RMB 43.96bn (+193% YoY) in Oct 2017 from just RMB 8-20bn in 1H17. For 10M17, Sunac's presales grew 142% YoY to RMB 249bn, equivalent to 83% of its annual target of RMB 300bn. For most developers, presales growth slowed in Oct 2017, but Sunac managed to accelerate sales further on increased saleable resources from M&A. We expect Sunac's FY17E presale to reach RMB 322bn (+114% YoY) and RMB 459bn (+42%YoY) for FY18E.

**Impressive M&A execution.** Sunac's fast-growing presales is driven by its expanding landbank via M&A. As of Aug 2017, Sunac's total landbank was 101mn sqm (39% higher than 72.9mn sqm in Dec 2016), excluding the recent acquisition of Wanda's 13 tourism projects with a GFA of 59mn sqm. About 71% of Sunac's landbank was acquired through M&A and the average land cost is RMB 5,130/sqm, representing only 30% of 10M17 presales ASP. Sunac is renowned for its proficient M&A execution, as proven by its numerous transactions (e.g. Greentown-Sunac JV and the latest Wanda acquisition). As market consolidation of PRC property sector continues, Sunac would capitalize on more M&A opportunities to further expand business.

**Margin recovery on track.** M&A has driven up Sunac's sales growth as well as its margin. GPM rebounded from 12.4% in 2015 to 13.7% in 2016 and 19.6% in 1H17. As Sunac reduces its participation in land auctions, the concern of overpriced land and margin erosion that used to associate with the Group gradually fades away. Regarding to the Wanda acquisition, Sunac acquired a 91% stake in 13 tourism projects at RMB 43.84bn for 49.7mn sqm of saleable GFA and 9.27mn sqm of self-owned GFA. Assuming a project debt of ~RMB 45bn to be taken up by Sunac, the average land cost of the asset portfolio is only ~RMB1,500/sqm. We expect these projects to entail a gross margin of ~40%, profit generated should more than offset the annual management fee of RMB 650mn (RMB 50mn per project) payable to Wanda.

#### Results and Valuation

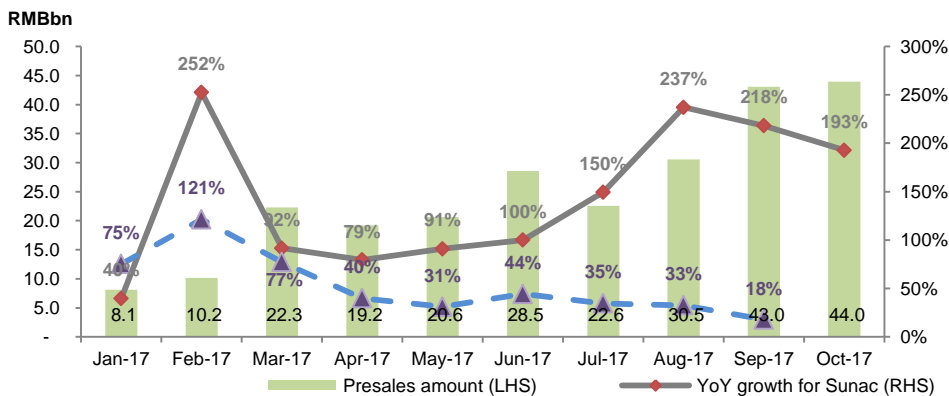
FY ended Dec 31	2015A	2016A	2017E	2018E	2019E
Revenue (RMB mn)	23,011	35,343	103,755	185,177	246,508
Chg (% YoY)	(8.2)	53.6	193.6	78.5	33.1
Core net profit (RMB mn)	3,377	1,532	4,100	8,718	14,839
Chg (% YoY)	(9.4)	(54.6)	167.6	112.7	70.2
Core EPS (RMB)	1.02	0.40	1.04	2.11	3.59
Chg (% YoY)	(9.4)	(61.0)	161.4	103.3	70.2
BVPS (RMB)	5.73	6.03	7.38	8.32	10.48
Chg (% YoY)	16.2	5.2	22.4	12.8	25.9
Core PE (x)	30.7	78.6	30.1	14.8	8.7
P/B (x)	5.4	5.2	4.2	3.8	3.0
ROE (%)	17.8	4.6	10.3	19.4	27.5
ROA (%)	2.9	0.5	0.6	0.9	1.3
DPS(RMB)	0.19	0.26	0.42	0.84	1.44
Yield (%)	0.6	0.8	1.3	2.7	4.6
Net gearing (%)	75.9	121.5	451.6	358.0	117.0

Source(s): Bloomberg, ABCI Securities estimates

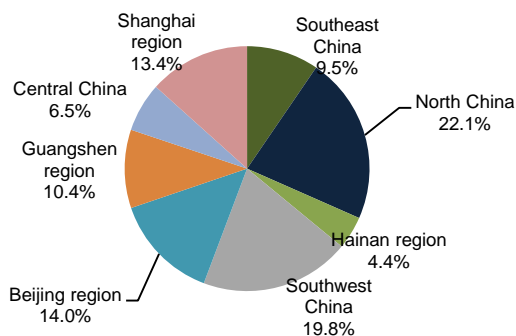
**Market voted “Yes” to Sunac’s highly-leveraged expansion strategy.** Sunac’s highly-g geared balance sheet used to be one of the major investor concerns. The Group’s net gearing soared 138ppt HoH to 260% as at June 2017, up 186ppt HoH to 393% if including perpetual as debt. Nonetheless, the Group’s share price has rallied 55% since its interim results announcement. Average daily turnover of Sunac’s shares in the past three months reached HK\$ 970mn, compared to HK\$ 74mn for 2016. The surging share price and stock trading liquidity is not solely driven by an increasing no. of mainland investors; in fact, stock-holding from China Securities Depository and Clearing (CSRC) via the Shanghai-HK connect declined from 22.58% of total share capital in Aug 2017 to 20.7% as at Nov 2017. We believe overseas investors, similar to the mainland ones, have turned more receptive to its highly-leveraged expansion strategy. On the credit side, Sunac’s bond yield was stable since its interim results announcement despite the dramatic increase in net gearing in 1H17.

**Upgrade to BUY and raise TP to HK\$ 42.2.** Factoring in the latest land acquisition and the Wanda transaction, we raise our 2018E NAV forecast to HK\$ 60.3/share (from HK\$ 24.1/share). We apply a 30% discount (from 60%), in line with the large-cap average discount, to derive our TP of HK\$ 42.20 (from HK\$ 9.70). Upgrade to **BUY** from Sell.

**Risk factors:** **1) Significant increase in SG&A costs:** The Wanda projects include tourism facilities such as Theme park and hotels, which require extra operating costs; **2) Corporate governance:** the listing committee censured Sunac and two Executive Directors for failure in ensuring the announcement regarding the Kaisa acquisition was accurate and complete; **3) Placement risk:** Sunac placed 220mn of new shares at HK\$ 18.33/share in July 2017. Sunac may conduct another round of share placement given the current share price level.

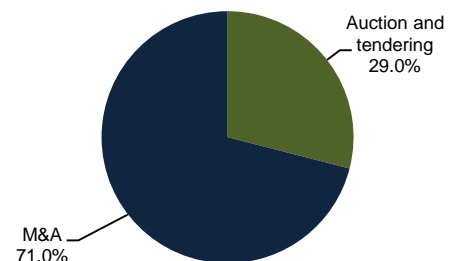
**Exhibit 1: Sunac’s monthly sales in 2017**


Source(s): Company, ABCI Securities

**Exhibit 2: Landbank by region (Aug 25, 2017: 101mn sqm)**


\* Excluded the Wanda acquisition

Source(s): Bloomberg, ABCI Securities

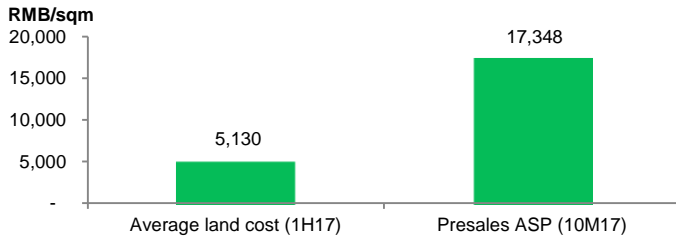
**Exhibit 3: Landbank by acquisition method (Aug 25, 2017: 101mn sqm)**


\* Excluded the Wanda acquisition

Source(s): Bloomberg, ABCI Securities

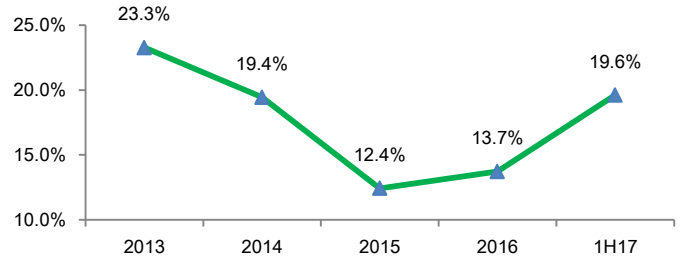


Exhibit 4: Average land cost vs. ASP in 10M17



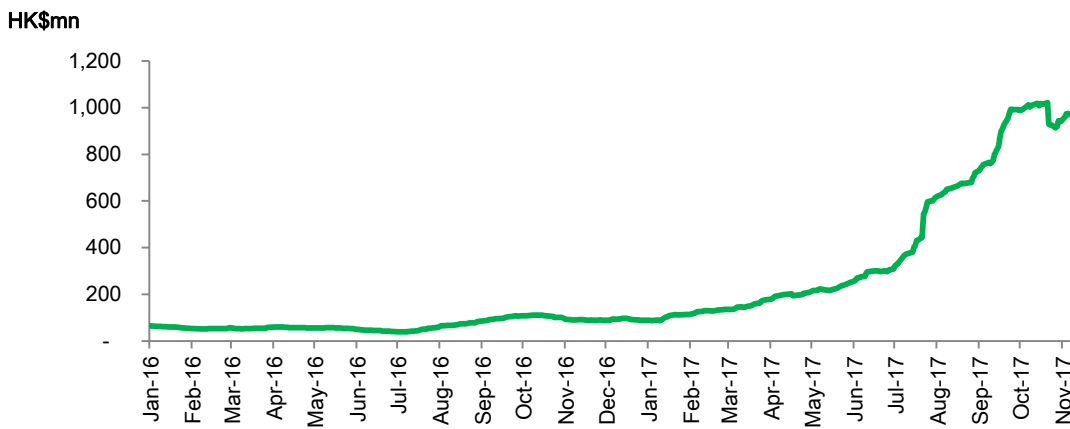
Source(s): Bloomberg, ABCI Securities

Exhibit 5: Gross margin trend



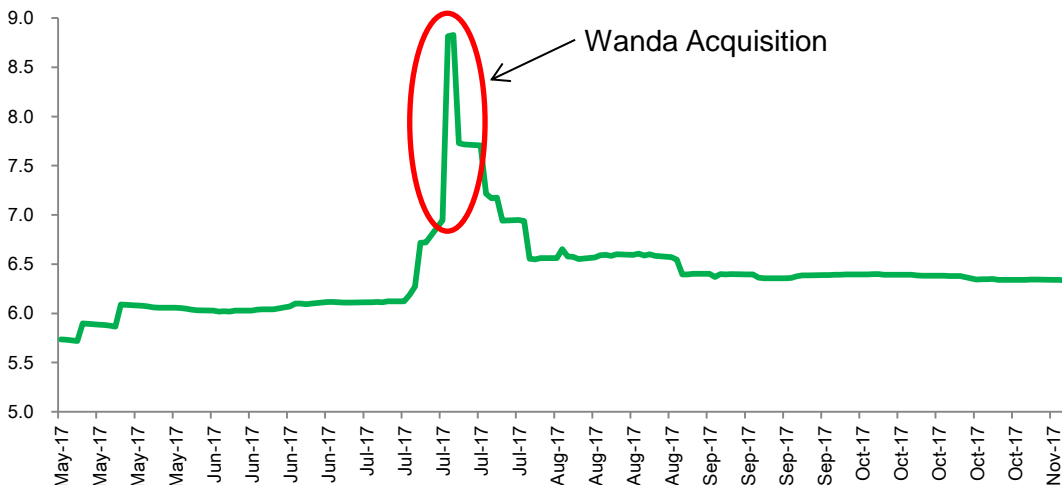
Source(s): Bloomberg, ABCI Securities

Exhibit 6: Three-month average daily turnover for Sunac



Source(s): Bloomberg, ABCI Securities

Exhibit 7: Bond yield of Sunac's 8.75% coupon USD bond maturing in 2019



Source(s): Bloomberg, ABCI Securities



**Exhibit 8: Sunac's 1H17 results recap**

P&L	1H17	1H16	YoY
	RMB mn	RMB mn	(%)
<b>Turnover</b>	13,333	10,586	25.9
Cost of Sales	(10,717)	(9,180)	16.7
<b>Gross Profit</b>	<b>2,616</b>	<b>1,406</b>	<b>86.0</b>
<b>Gross Margin (%)</b>	<b>19.6</b>	<b>13.3</b>	<b>+6.3ppt</b>
Selling and distribution costs	(779)	(319)	144.7
Administrative expense	(1,017)	(476)	113.7
<b>EBIT</b>	<b>819</b>	<b>612</b>	<b>34.0</b>
<b>EBIT Margin (%)</b>	<b>6.1</b>	<b>5.8</b>	<b>+0.3ppt</b>
Other income	1,026	594	72.6
Share of profit from JCE/ Assoc.	(397)	(236)	68.6
Exceptional items	2,699	1,055	155.8
Exchange losses and others	66	(600)	(111.0)
Finance cost	(2,073)	(979)	111.9
<b>Profit before tax</b>	<b>2,140</b>	<b>447</b>	<b>378.6</b>
<b>Tax</b>	<b>(395)</b>	<b>(344)</b>	<b>14.6</b>
- LAT	(682)	(702)	(2.9)
- Enterprise tax	287	(309)	(192.8)
<b>Profit after tax</b>	<b>1,745</b>	<b>103</b>	<b>1,598.4</b>
Minority Interest	(314)	(30)	951.3
<b>Net profit</b>	<b>1,432</b>	<b>73</b>	<b>1,863.1</b>
<b>Core net profit</b>	<b>(642)</b>	<b>(269)</b>	<b>139.1</b>

Operating statistics	1H17	1H16	YoY
			%
Contracted GFA (mn sqm)	5.95	2.83	110.8
Contracted ASP (RMB/sqm)	18,282	19,841	(7.9)
<b>Contracted Sales (RMB mn)</b>	<b>108,850</b>	<b>56,050</b>	<b>94.2</b>
GFA Delivered (mn sqm)	0.89	0.63	40.7
Booked ASP (RMB/sqm)	14,519	16,424	(11.6)
<b>Booked sales (RMB mn)</b>	<b>12,861</b>	<b>10,337</b>	<b>24.4</b>
<b>Balance sheet</b>	<b>Jun-17</b>	<b>Dec-16</b>	<b>YoY</b>
	RMB mn	RMB mn	
Gross debt	181,297	112,844	60.7
Cash	92,409	69,813	32.4
<b>Net debt</b>	<b>88,888</b>	<b>43,031</b>	<b>106.6</b>
<b>Net gearing (%)</b>	<b>259.6</b>	<b>121.5</b>	<b>+138.1ppt</b>
<b>Net gearing (%) - perpetual</b>	<b>393.9</b>	<b>208.2</b>	<b>+185.7 ppt</b>

Source(s): Company, ABCI Securities

**Exhibit 9: Sunac's 2018E NAV**

	Attr. GFA (mn sqm)	Net assets value (RMB mn)	% of total	Valuation Method	Implied value per sqm (RMB)
Property development	177.6	400,392	94%	DCF at WACC of 10.5%	2,255
Property investment & management		1,282	0%	6.5% cap rate on 2017E net rental & mgt. fee	
Investment in Leshi		13,941	3%	Historical cost	
Investment in Homelink		2,800	1%	Historical cost	
Investment in Jinke Properties		6,976	2%	Market value	
<b>Total 2018E GAV</b>		<b>425,390</b>	<b>100%</b>		
2018E Net cash/ (debt)		(203,869)	-41%		
2018E Perpetual instrument		(10,609)	-2%		
<b>Total 2018E NAV</b>		<b>210,912</b>	<b>56%</b>		
No. of share outstanding (diluted)		4,130			
<b>NAV per share (RMB)</b>		<b>51.1</b>			
Ex rate		1.18			
<b>NAV per share (HKD)</b>		<b>60.3</b>			
Target discount (%)		30%			
<b>Target Price (HKD)</b>		<b>42.20</b>			
<b>WACC</b>	<b>10.5%</b>				
Cost of debt	8.0%				
Cost of equity	20.0%				
<b>Debt/ ( Debt + Equity)</b>	<b>68%</b>				

Source(s): Company, ABCI Securities estimates



**Consolidated income statement (2014A-2019E)**

<b>FY Ended Dec 31 (RMB mn)</b>	<b>2014A</b>	<b>2015A</b>	<b>2016A</b>	<b>2017E</b>	<b>2018E</b>	<b>2019E</b>
<b>Revenue</b>	25,072	23,011	35,343	103,755	185,177	246,508
Cost of sales	(20,197)	(20,154)	(30,495)	(83,120)	(149,677)	(200,769)
<b>Gross Profit</b>	4,875	2,857	4,848	20,635	35,499	45,739
SG&A expenses	(1,378)	(1,364)	(1,649)	(3,985)	(6,330)	(6,009)
<b>EBIT</b>	3,497	1,493	3,199	16,651	29,170	39,730
Finance cost	(1,267)	(1,720)	(2,472)	(4,448)	(6,248)	(6,368)
Share of profit of associates	2,181	1,693	836	1,313	865	516
Other income/ (expenses)	908	1,353	1,584	2,385	2,364	2,626
Fair value gain of investment properties	-	-	-	-	-	-
Disposal/one-off items	(417)	1,745	1,262	-	-	-
<b>Profit before tax</b>	4,902	4,564	4,409	15,901	26,150	36,504
Tax	(1,669)	(955)	(1,470)	(6,969)	(10,484)	(13,383)
<b>Profit after tax</b>	3,233	3,608	2,938	8,931	15,665	23,120
Minority interest	(11)	(311)	(157)	(3,877)	(5,992)	(7,327)
Perpetual coupon distribution	-	-	(303)	(955)	(955)	(955)
<b>Reported net profit</b>	3,222	3,298	2,478	4,100	8,718	14,839
Less: exceptional items	507	79	(946)	-	(0)	(0)
<b>Underlying net profit</b>	3,729	3,377	1,532	4,100	8,718	14,839
<b>Per share</b>						
Underlying EPS (RMB)	1.12	1.02	0.40	1.04	2.11	3.59
DPS (RMB)	0.19	0.19	0.26	0.42	0.84	1.44
Payout ratio (%)	17%	19%	65%	40%	40%	40%
BVPS (RMB)	4.93	5.73	6.03	7.38	8.32	10.48
<b>Growth %</b>						
Revenue	-18.7%	-8.2%	53.6%	193.6%	78.5%	33.1%
Gross Profit	-32.1%	-41.4%	69.7%	325.6%	72.0%	28.8%
EBIT	-42.1%	-57.3%	114.2%	420.5%	75.2%	36.2%
Underlying net profit	5.9%	-9.4%	-54.6%	167.6%	112.7%	70.2%
<b>Margin %</b>						
Gross margin	19.4%	12.4%	13.7%	19.9%	19.2%	18.6%
Gross margin (post-LAT)	16.3%	14.3%	12.0%	16.2%	16.4%	16.3%
EBIT margin	13.9%	6.5%	9.1%	16.0%	15.8%	16.1%
Core net margin	5.4%	2.6%	2.4%	6.4%	7.5%	8.8%
<b>Key assumptions</b>						
Contracted Sales (RMB mn)	65,800	68,143	150,523	333,164	475,903	441,799
GFA sold (mn sqm)	3.10	3.50	7.58	20.73	30.36	29.35
ASP (RMB/sqm)	21,246	19,477	19,865	16,075	15,674	15,052
Booked Sales (RMB mn)	24,719	22,511	34,611	102,986	184,369	245,660
GFA delivered (mn sqm)	1.65	1.39	2.16	6.03	11.40	15.77
Booked ASP (RMB/sqm)	15,009	16,226	16,013	17,086	16,168	15,579

Source(s): Company, ABCI Securities estimates



**Consolidated balance sheet (2014A-2019E)**

As of Dec 31 (RMB mn)	2014A	2015A	2016A	2017E	2018E	2019E
<b>Current assets</b>	97,467	93,725	252,698	607,041	851,611	1,038,873
Cash	20,657	22,687	52,086	33,450	41,248	164,539
Restricted cash	4,384	4,371	17,727	17,727	17,727	17,727
Trade & other receivables	2,475	970	8,416	8,416	8,416	8,416
Property under development	49,383	49,870	130,621	503,601	740,373	804,344
Other current assets	20,568	15,826	43,847	43,847	43,847	43,847
<b>Non-current assets</b>	14,895	21,784	40,485	60,404	80,849	101,224
Property, plant & equipment	62	69	547	539	20,511	40,483
Investment properties	239	-	656	656	656	656
Investment in Associate and JCE	12,049	15,261	34,553	54,480	54,952	55,356
Other non-current assets	2,546	6,455	4,730	4,730	4,730	4,730
<b>Total Assets</b>	112,362	115,509	293,183	667,445	932,460	1,140,098
<b>Current Liabilities</b>	64,949	64,495	168,594	532,500	786,342	977,798
Short-term borrowings	13,840	14,584	32,644	177,644	182,644	187,644
Trade & other payables	11,616	10,944	41,413	41,413	41,413	41,413
Pre-sales deposits	12,271	13,420	34,376	253,282	502,124	688,581
Other current liabilities	27,223	25,546	60,160	60,160	60,160	60,160
<b>Non-current liabilities</b>	26,431	31,594	89,178	89,178	89,178	89,178
Long-term borrowings	20,544	27,214	80,200	80,200	80,200	80,200
Other payables	-	-	-	-	-	-
Other non-current liabilities	5,887	4,379	8,978	8,978	8,978	8,978
<b>Total Liabilities</b>	91,380	96,089	257,772	621,677	875,519	1,066,976
<b>Net Assets</b>	20,983	19,420	35,411	45,768	56,941	73,122
<b>Shareholders' Equity</b>	16,353	19,005	23,269	29,147	34,378	43,282
Perpetual capital instrument	-	-	9,957	10,609	10,609	10,609
Minority Interest	4,630	415	2,185	6,012	11,954	19,230
<b>Total Equity</b>	20,983	19,420	35,411	45,768	56,941	73,122
<b>Key ratio</b>						
Gross debt (RMB mn)	34,384	41,799	112,844	257,844	262,844	267,844
Net debt (RMB mn)	9,342	14,740	43,031	206,668	203,869	85,578
Net gearing (%)	45%	76%	122%	452%	358%	117%
Contracted sales/ Total assets (x)	59%	59%	51%	50%	51%	39%

Source(s): Company, ABCI Securities estimates



Consolidated cash flow statement (2014A-2019E)

FY ended Dec 31 (RMB mn)	2014A	2015A	2016A	2017E	2018E	2019E
EBITDA	3,522	1,521	3,227	16,679	29,198	39,758
Change in Working Capital	6,227	4,204	(43,290)	(143,695)	26,649	137,345
Tax payment	(1,669)	(955)	(1,470)	(6,969)	(10,484)	(13,383)
<b>Operating cash flow</b>	<b>8,080</b>	<b>4,770</b>	<b>(41,534)</b>	<b>(133,985)</b>	<b>45,363</b>	<b>163,719</b>
Purchase of PP&E	(20)	(20)	(20)	(20)	(20,000)	(20,000)
Addition of Investment Properties	-	-	-	-	-	-
Others	1,353	6,319	(1,847)	(16,229)	2,755	2,739
<b>Investing cash flow</b>	<b>1,333</b>	<b>6,299</b>	<b>(1,867)</b>	<b>(16,249)</b>	<b>(17,245)</b>	<b>(17,261)</b>
Debt raised	10,760	9,057	74,017	150,000	10,000	10,000
Debt repaid	(9,214)	(15,000)	(5,000)	(5,000)	(5,000)	(5,000)
Interest expenses	(3,036)	(2,948)	(4,479)	(14,828)	(20,828)	(21,228)
Equity raised	-	-	2,478	3,417	-	-
Dividend to shareholders	(630)	(643)	(991)	(1,640)	(3,487)	(5,935)
Others	(50)	495	6,775	(353)	(1,005)	(1,005)
<b>Financing cash flow</b>	<b>(2,170)</b>	<b>(9,039)</b>	<b>72,800</b>	<b>131,597</b>	<b>(20,319)</b>	<b>(23,168)</b>
<b>Net cash inflow/ (outflow)</b>	<b>7,243</b>	<b>2,030</b>	<b>29,399</b>	<b>(18,636)</b>	<b>7,799</b>	<b>123,291</b>
Cash- beginning	13,414	20,657	22,687	52,086	33,450	41,248
<b>Cash- year-end</b>	<b>20,657</b>	<b>22,687</b>	<b>52,086</b>	<b>33,450</b>	<b>41,248</b>	<b>164,539</b>

Source(s): Company, ABCI Securities estimates

## Disclosures

### Analyst Certification

I, Kenneth Tung, being the person primarily responsible for the content of this research report, in whole or in part, hereby certify that all of the views expressed in this report accurately reflect my personal view about the subject company or companies and its or their securities. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed in this report. I and/or my associates have no financial interests in relation to the listed company (ies) covered in this report, and I and/or my associates do not serve as officer(s) of the listed company (ies) covered in this report.

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### Definition of equity rating

Rating	Definition
Buy	Stock return $\geq$ Market return rate
Hold	Market return $- 6\% \leq$ Stock return $<$ Market return rate
Sell	Stock return $<$ Market return $- 6\%$

Stock return is defined as the expected % change of share price plus gross dividend yield over the next 12 months

Market return: 5-year average market return rate

Time horizon of share price target: 12-month

### Definition of share price risk

Rating	Definition
Very high	$2.6 \leq$ 180 day volatility/180 day benchmark index volatility
High	$1.5 \leq$ 180 day volatility/180 day benchmark index volatility $<$ 2.6
Medium	$1.0 \leq$ 180 day volatility/180 day benchmark index volatility $<$ 1.5
Low	180 day volatility/180 day benchmark index volatility $<$ 1.0

We measure share price risk by its volatility relative to volatility of benchmark index. Benchmark index: Hang Seng Index.

Volatility is calculated from the standard deviation of day to day logarithmic historic price change. The 180-day price volatility equals the annualized standard deviation of the relative price change for the 180 most recent trading days closing price.

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